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No. 816

In the Supreme Court of the United States

October Term, 1940

GUY T. HELVERING, Commissioner of Internal Revenue, Petitioner,

v.

O. G. HARMEL

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE PETITIONER

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In the Supreme Court of the United States

OCTOBER TERM, 1940

No. 516

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

O. G. RICHTER

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE PETITIONER

OPINIONS BELOW

The memorandum opinion of the United States Board of Tax Appeals (R. 16–17) is not reported. The opinion of the Circuit Court of Appeals for the Third Circuit (R. 28–30) is reported in 114 F. (2d) 452.

JURISDICTION

The judgment of the United States Circuit Court of Appeals was entered on July 17, 1940 (R. 30). The petition for a writ of certiorari was filed on October 17, 1940, and was granted on November 18, 1940, limited to the first of the two questions presented. The jurisdiction of this Court rests upon Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

The taxpayer transferred securities to a third party in trust to pay the income to his wife. At the end of five years, or earlier if the wife consented, or on the death of the taxpayer or his wife, the securities were to be transferred back to the taxpayer. The Board of Tax Appeals held that the grantor was not taxable with respect to the income from the trust. Only one question is here presented:

Whether, by invoking the general gross income provisions of Section 22, the Commissioner had so changed the theory of the Government's case on appeal as to preclude the Circuit Court of Appeals from considering the issue.

STATUTES AND REGULATIONS INVOLVED

The relevant provisions of the statutes and regulations involved are set forth in the Appendix E, *infra*, pp. 61–70.

STATEMENT

The facts stipulated by the parties (R. 8–16) were adopted by the Board of Tax Appeals as its findings of fact (R. 16). They may be summarized as follows:

By a trust instrument dated December 29, 1930, the taxpayer placed a group of securities in trust with the Union Trust Company of Pittsburgh, to pay, during the duration of the trust, the net income of the trust to Nannie C. Richter, the tax-

payer's wife, in such installments as she might request.

Unless revoked sooner, either by the act of the taxpayer with the consent of the beneficiary, or by death of the taxpayer or the beneficiary, the trust was to terminate on January 3, 1936; upon termination, the original corpus plus subsequent additions thereto was to be delivered to the taxpayer free of the trust (R. 11–12).

By instrument dated June 3, 1932 (R. 15–16), the taxpayer extended the term of the trust to January 3, 1938, provided that the trust was not sooner terminated by act of the taxpayer with the consent of the beneficiary, or by death of the taxpayer or beneficiary. The taxpayer did not at any time have any agreement with his wife that she would join with him upon his request for a termination of the trust prior to the time specified for its termination. Taxpayer at no time asked his wife to join in an agreement for termination, and she at no time offered to join with him in any agreement for termination. Taxpayer's wife died on November 26, 1935 (R. 9, 10).

The trust was in effect throughout the year 1934, and the trustee paid the entire net income of the trust for that year to taxpayer's wife (R. 9–10). In determining the income tax liability of the taxpayer for the calendar year 1934, the Commissioner

attributed the income of the trust to the taxpayer and determined a deficiency accordingly (R. 4–7).[1]

The taxpayer petitioned for a redetermination of of the deficiency by the Board of Tax Appeals, asserting that "The Commissioner of Internal Revenue erred in including in the income of petitioner the net income arising under the trust established by the petitioner on December 29, 1930, as amended June 3, 1932, the beneficiary of which was his wife, Nannie C. Richter" (R. 3). The Commissioner in his answer denied the alleged error (R. 8). A stipulation of facts was filed on December 6, 1938, reserving to each party "the right to introduce any other evidence not inconsistent therewith" (R. 1, 8–16), and the time for filing briefs was set as follows: "Petitioner's brief due 1/5/39. Commissioner's brief due 2/4/39. Petitioner's reply due 2/20/39". (R. 1).

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[1] The Commissioner in his ninety-day deficiency letter, stated (R. 7):

"EXPLANATION OF CHANGES

"In accordance with the recommendation of the revenue agent, your return has been adjusted to include the net income of the trust created by you in 1930 for the benefit of your wife, Nannie C. Richter.

"The record indicates that under the provisions of section 166 of the Revenue Act of 1934 the trust created by you in 1930 for the benefit of your wife, Nannie C. Richter, was a revocable trust and, therefore, the net income is taxable to the grantor. In accordance with the provisions of the trust instrument, the trust could be terminated by you at any time with consent of the beneficiary and the title to the corpus would revest in the grantor upon the exercise of such power. The trust terminated on January 3, 1936, the corpus reverting to the grantor."

The Commissioner in his brief undertook to defend his determination on two grounds: (1) That the income was taxable to the grantor under Section 166 of the Revenue Act of 1934; and (2) that the grantor retained such substantial incidents of ownership in the corpus as to render him taxable upon the income therefrom under Article 166–1 of Regulations 86, as amended by Treasury Decision 4629 (1936). Appendix A, *infra*, pp. 54–55. The taxpayer in his reply brief stated (Appendix B, *infra*, p. 57):

> It is to be noted that, in the Commissioner's deficiency letter (Petition, paragraph 2 and Exhibit A thereto), the position was taken that the trust involved "was a revocable trust and, therefore, the net income is taxable to the grantor." The respondent seems to have definitely abandoned the position that this is a revocable trust, * * *.

The taxpayer then discussed the merits of the Commissioner's position, as follows (Appendix B, *infra*, p. 57): [2]

> The next step [in the Commissioner's argument] * * * is that there was a regulation

[2] Later, the taxpayer added: "As sought to be applied by the respondent in this case, Regulations 86 ignore completely the language of the Congress, whereby it provided for the taxability of the income arising under a trust where the grantor 'had the power', and fail utterly, if the present interpretation thereof sought to be applied be correct, to distinguish between the 'termination' of the trust by its own terms and the 'revocation' of the trust by some unfettered act of the grantor before its automatic termination under express provisions of the trust instrument." Appendix B, *infra*, p. 58.

> in effect in 1934 (part of Article 166–1, Regulations 86) providing that the grantor is regarded as in substance the owner of the corpus if it is apparent that he has failed to part permanently and definitively with the substantial incidents of ownership in the corpus, and that, the petitioner being in substance the owner of the corpus because it will ultimately come back to him, the income is taxable to him. The answer to this proposition is plain: The regulation as sought to be applied in this case goes beyond the pertinent statutory provision itself, and, seeking to make taxable what was expressly excluded from taxation by the statute itself, is null and void. * * *

The Board held the taxpayer-grantor was not taxable.

Upon appeal to the Circuit Court of Appeals, the Commissioner again urged not only that the grantor was taxable under Section 166 of the 1934 Act, but also that the income was attributable to him under Article 166–1 of Regulations 86, as amended by Treasury Decision 4629 (1936) (R. 20, 23). However, subsequently, as a result of this Court's supervening decisions in *Helvering* v. *Clifford*, 309 U. S. 331, and *Helvering* v. *Wood*, 309 U. S. 344, the Commissioner waived reliance upon Section 166, but sought to have the income taxed under Section 22 (a), which contained the statutory provisions supporting Article 166–1 of Regulations 86, as amended by Treasury Decision 4629 (1936), previously relied upon. Appendix C, *infra*, p. 59. The Circuit Court of Appeals refused to consider Section 22 (a) on the theory that it was being raised for the first

time on appeal, and affirmed the decision of the Board (R. 29, 30).

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding and deciding that the income derived from the Nannie C. Richter Trust during the calenday year 1934 was not taxable to the grantor, O. G. Richter.

2. In failing to hold and decide that the income of the Nannie C. Richter Trust for the calendar year 1934 was taxable to the grantor as his income in the year 1934.

3. In failing to hold that the trust income was taxable to the grantor under Article 166–1 of Treasury Regulations 86, as amended.

4. In failing to hold that the foregoing provisions of Article 166–1 are supported by Section 22 (a) of the Revenue Act of 1934.

5. In holding that the applicability of Section 22 (a), *supra*, involved a new issue which could not be presented on appeal.

6. In failing to hold that the taxability of the trust income to the grantor was, in a broad sense, the issue before the Board of Tax Appeals.

7. In failing to reverse the decision of the Board of Tax Appeals.

SUMMARY OF ARGUMENT

I

The Government under a separate heading in its brief before the Board argued that the taxpayer had

failed to part definitively with the substantial incidents of ownership in the corpus and should be regarded as remaining in substance the owner of the corpus of the trust within the meaning of Article 166–1 of Regulations 86 as amended by Treasury Decision 4629 (1936). The taxpayer did not object to the Board's consideration of the issue or theory of substantial ownership. His reply brief first observes that the Commissioner "seems to have definitely abandoned the position that this is a revocable trust * * *." It then states and answers on the merits the broader position taken by the Commissioner before the Board. At no time did the taxpayer contend before the Board that he was prejudiced or surprised by the Commissioner's reliance upon this broad issue of substantial ownership.

The ninety-day letter of the Commissioner, it is true, explains the deficiency by stating only that under Section 166 the trust was a revocable trust. But it is clear beyond doubt that the reasons given in the Commissioner's deficiency letter in no way limit the issues or theories that may be raised before the Board. The question there is not whether the Commissioner's course of reasoning was correct but whether his determination was correct, irrespective of the reasons advanced to support it.

The Board's rules of practice show that the issues on an appeal are determined by the pleadings of the parties. The petition and answer in this case disclose that the issue before the Board was the broad question whether the trust income was taxable to the taxpayer-settlor. The subsequent hearing and argu-

ment offered opportunity to the parties to adduce the facts and present their legal theories with respect to them. But in this case the hearing was merely *pro forma:* the facts had been stipulated in advance, and the stipulation was admitted into evidence at the hearing without argument or explanation. The briefs filed with the Board, therefore, presented the first occasion for either party to crystallize the legal theories with respect to the transaction of trust under consideration. From the standpoint of settled Board practice, the propriety of advancing a theory for the first time in a brief filed with the Board cannot be doubted. Moreover, the Board's opinion nowhere states in terms that the broad theory of substantial ownership was not raised before it.

Article 166–1 of Regulations 86 as amended in 1936 was, unless invalid, fully applicable to the tax year in question. The Revenue Act of 1934 under which Regulations 86 were promulgated governs only the years 1934 and 1935. The 1936 amendment to these regulations would therefore have been entirely without meaning unless it were to apply to the years 1934 and 1935. The scheme of the revenue acts, moreover, contemplates that changes in the regulations are to relate to all tax years governed by the regulations unless the Secretary of the Treasury or the Commissioner affirmatively provides that the change shall have only prospective application.

There is no basis in reason for regarding Article 166–1 as amended in 1936 other than as valid. The criteria there stated to be controlling created no

new rule of liability. The 1936 amendment, by relying upon Section 22 (a), merely sharpened the legal theory upon which income theretofore attributed to the taxpayer-grantor of a trust was to be included in his gross income. *Helvering* v. *Clifford*, 309 U. S. 331, shows that the amended article, as well as the original, is well within the area of discretion conferred by Congress on the Commissioner.

Helvering v. *Wood*, 309 U. S. 344, is not controlling here. In the circumstances there presented the Commissioner could well be deemed to have narrowed the issue to the construction of Section 166 and to have abandoned the theory of substantial ownership except insofar as supported by Section 166. The cases cited and the reasoning followed in the opinion indicate that the *Wood* decision was intended to govern only the practice in this Court, not the practice in the circuit courts of appeals. The emphasis in the opinion upon the *waiver* in the circuit court of appeals suggests that in the absence of such waiver, as in the case here, the point would have been open both in that court and in this Court. In the case at bar, on the contrary, the theory of substantial ownership embodied in Article 166–1 as amended was never narrowed or abandoned but was fully argued before the Board. The Commissioner upon appeal may therefore advance a new reason—Section 22 (a)—to support the validity of his regulations.

It is likewise clear that the court below should have considered Section 22 (a) as construed in *Helvering*

v. *Clifford*, 309 U. S. 331. The amended regulations upon which the Commissioner relied both before the Board and the Circuit Court of Appeals rest in part upon Section 22 (a). They also express the same theory as to tax liability which is expressed by Section 22 (a) as construed in the *Clifford* case. It may be noted, moreover, that Section 22 (a) would be before the Circuit Court of Appeals even were the amended regulations declared invalid. The Commissioner, whether justified or not, did place his reliance upon the amended regulations. By so doing, he framed the issue in terms as broad as that framed by Section 22 (a) and gave notice, to all who read the amended regulations, that the ultimate statutory basis for taxability was other than Section 166.

II

The result should be the same even though it be assumed, for purposes of argument, that "the issue presented to the Board was whether Section 166 applied to a trust in which the estate reverted to the settlor after a period of years" and that "the stipulated facts were framed with this issue in view." The Government contends that even so the court below had power to dispose of the case under Section 22 (a) and, in the circumstances, should be directed to exercise that power.

This Court has settled that an appellee may support the determination of the Board of Tax Appeals upon a new issue, raised for the first time upon

appeal, even though the consideration of that issue requires that the case be remanded. *Helvering* v. *Gowran*, 302 U. S. 238, 245–246, and cases therein cited. One may therefore question the existence of any blanket rule denying that there is power to consider a new issue raised on appeal by an appellant. The decisions of the Court also show that it has no want of power to reverse a judgment under review upon a theory not theretofore presented. A recent example in the tax field is *Helvering* v. *Leonard*, 310 U. S. 80, 83. Another situation in which this has been done is shown by *Erie R. R. Co.* v. *Tompkins*, 304 U. S. 64, and *Ruhlin* v. *New York Life Ins. Co.*, 304 U. S. 202. During this Term the Court has asserted its power to consider errors of a fundamental nature whether raised or not. *Sibbach* v. *Wilson & Company, Inc.*, No. 28, this Term, and cases therein cited. And the rule has been laid down that a supervening change in law or fact is substantial ground for reversing a judgment right when made. *Vandenbark* v. *The Owens-Illinois Glass Co.*, No. 141, this Term, and cases therein cited; *Gulf, Colorado & S. F. Ry.* v. *Dennis*, 224 U. S. 503, and cases therein cited. A somewhat analogous practice is found in the settled rule that this Court, without finally disposing of a case, has power to remand the case where the trial was had upon the wrong theory or the record does not permit of final disposition with justice to all parties. E. g., *United States* v. *Shelby Iron Co.*, 273 U. S. 571, 579; *United States* v. *Rio Grande Dam Co.*, 184 U. S.

416, 423; 215 U. S. 266, 275; *Combs* v. *Hodge*, 21 How. 397, 408.

This Court has never laid down a blanket rule prohibiting a circuit court of appeals from considering any issue except one fully argued before the Board. *General Utilities Co.* v. *Helvering*, 296 U. S. 200, stands for no such proposition. The opinion there refers to the merits of the new issue not argued before the Board and indicates that, unless the Commissioner's position is lacking in merit, the case may be remanded to the Board for disposition upon the correct rule of law. Accord: *Helvering* v. *Salvage*, 297 U. S. 106, 107. Reversal of the Board upon a new issue is supported by the statutory command that, "if the decision of the Board is not in accordance with law," the circuit court of appeals shall have power to dispose of the case "as justice may require". Compare *Helvering* v. *Taylor*, 293 U. S. 507; *Legg's Estate* v. *Commissioner*, 114 F. (2d) 760, 767 (C. C. A. 4th). The existence of the power to reverse a decision of the Board upon a new issue or theory has been affirmed on numerous occasions by the various circuit courts of appeals. *Legg's Estate* v. *Commissioner*, 114 F. (2d) 760, 767 (C. C. A. 4th), and cases therein cited.

The Circuit Court of Appeals, assuming it has the power, should be directed to dispose of this case under Section 22 (a). The situation here (viewed most favorably to the taxpayer) discloses that a theory of liability—substantial ownership under

Section 22 (a)—which might have been raised either by the parties or the Board was overlooked and not directly called to the Board's attention. Since its disposition of the case, however, a supervening decision of this Court has shown that this theory beyond doubt is applicable and probably is determinative of the merits in favor of the Commissioner.

The leading authority as to the correct practice to be followed by the circuit courts of appeals—the *General Utilities* case—lends support to our position. By referring to the merits of the new issue, the opinion indicates that, even in the situation there disclosed, the proceeding may be remanded to the Board in the event the Commissioner's position is meritorious. Compare *Helvering* v. *Salvage*, 297 U. S. 106, 109. The case, in any event, does not militate against us. The issue there sought to be raised required an investigation of a transaction distinct from the transaction relevant to the issue before the Board and required "an inference of fact directly in conflict with the stipulation of the parties and the findings." Here, quite to the contrary, a disposition of the case under Section 22 (a) may be made without the investigation of any transaction other than the transaction of trust considered by the Board and without the consideration of any facts other than the stipulated facts and findings. This case, therefore, comes directly within the rationale of numerous cases in the circuit courts of appeals where the Commissioner was sustained upon a new

theory predicated upon the facts in the record as to the transaction under consideration.

Finally, we submit, the instances in which this Court has ordered that disposition of a case be made in the light of a supervening decision, or change in the law or in the facts, are ample warrant for our position in the case at bar. *Blair* v. *Commissioner*, 300 U. S. 5; *Vandenbark* v. *The Owens-Illinois Glass Co.*, No. 141, this Term, and cases therein cited. The action of the parties and the Board shows that, even though embodied in the regulations, the theory of liability spelled out in the *Clifford* case was not well understood or established at the time of the Board hearing. The *Clifford* decision is therefore comparable in all essential respects to the supervening decisions relied upon in numerous cases before this Court.

ARGUMENT

The Government took the position before the Circuit Court of Appeals that under Section 22 (a) of the Revenue Act of 1934 the income from the trust for his wife was taxable to the taxpayer-settlor. Its contention was not given consideration. Instead, the Government was told, in effect, that the taxpayer's liability, even if it could be proved beyond a doubt, was forever barred because the transaction under consideration was presented to the Board of Tax Appeals upon the issue "whether section 166 applied to a trust in which the estate reverted to the settlor after a period of years" (R. 29). The

Circuit Court of Appeals reached this result without specific mention of what other facts, if any, could possibly have been brought forward by the taxpayer (at the original hearing before the Board) adequate to overcome the effect of the stipulated facts and avoid taxability under Section 22 (a).

The Government's argument here is twofold: we contend (1) that the issue or theory that the taxpayer-settlor should be "regarded as remaining in substance the owner of the corpus" presented by Article 166–1 as amended and by Section 22 (a) [3] was raised and argued before the Board and was properly before the Circuit Court of Appeals; and (2) that, in any event, the Circuit Court of Appeals could and should have considered and disposed of the case under Section 22 (a).

I

THE THEORY PRESENTED BY ARTICLE 166–1 AS AMENDED AND BY SECTION 22 (A) WAS RAISED AND ARGUED BEFORE THE BOARD AND WAS PROPERLY BEFORE THE CIRCUIT COURT OF APPEALS

1. The Government under a separate heading [4] in its brief before the Board opened its argument with the following statement (Appendix A, *infra*, pp. 54–55):

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[3] The Circuit Court of Appeals stated (R. 29): "Under Section 22 (a) the issue presented is whether the grantor after the establishment of the trust may still be treated as the owner of the corpus."

[4] The heading reads:

"*The provisions of Article 166–1 of Regulations 86, as amended, require that the income of the present trust be taxed to petitioner.*"

The facts of the instant case bring them squarely within the scope of Article 166–1 of Regulations 86, as amended by Treasury Decision 4629, *supra*, and specifically that part of the regulations which provides as follows:

"But the provisions of section 166 are not to be regarded as excluding from taxation to the grantor the income of other [5] trusts, not specified therein, in which the grantor is, for the purposes of the Act, similarly regarded as remaining in substance the owner of the corpus. The grantor is regarded as in substance the owner of the corpus if, in view of the essential nature and purpose of the trust, it is apparent that the grantor has failed to part permanently and definitively with the substantial incidents of ownership in the corpus."

It is apparent from the nature of the trust that petitioner has failed to part permanently and definitively with the substantial incidents of ownership in the corpus of the trust. * * * [The Commissioner then urged that the regulations were reasonable and supportable under Section 166 and that they were applicable to the facts of this case.]

The portions thus quoted from Regulations 86 show on their face that Article 166–1 as amended is not based solely upon Section 166 nor confined to the

[5] In a preceding paragraph, Article 166–1 as amended states (Appendix E, *infra*, p. 62):

"(b) Section 166 defines with particularity instances in which the grantor is regarded as in substance the owner of the corpus by reason of the fact that he has retained power to revest the corpus in himself. * * *"

types of trusts therein specified. Rather, as this Court recognized in *Helvering* v. *Clifford*, 309 U. S. 331, 334n., they show that "Article 166–1 of Treasury Regulations 86 promulgated under § 166 of the 1934 Act" was "in 1936 amended (T. D. 4629) so as to rest on § 22 (a) also." Moreover, even a casual reading of the amended regulations discloses the following description of the governing criteria (Appendix E, *infra*, p. 63):

> In determining whether the grantor is in substance the owner of the corpus, the Act has its own standard, which is a substantial one, dependent neither on the niceties of the particular conveyancing device used, nor on the technical description which the law of property gives to the estate or interest transferred to the trustees or beneficiaries of the trust. In that determination, among the material factors are: the fact that the corpus is to be returned to the grantor after a specific term; the fact that the corpus is or may be administered in the interest of the grantor; the fact that the anticipated income is being appropriated in advance for the customary expenditures of the grantor or those which he would ordinarily and naturally make; and any other circumstances bearing on the impermanence and indefiniteness with which the grantor has parted with the substantial incidents of ownership in the corpus.

These criteria are then illustrated so as to leave no doubt as to their applicability to the case at bar, as follows (Appendix E, *infra*, p. 64):

> (c) For example, a grantor is regarded as remaining in substance the owner of the corpus of the trust, if he has placed it in trust for his son, John.
>
> "(A) for the term of three years, at the end of which time the trust might be extended for a like period at the option of the grantor and successively thereafter, but in the absence of such an extension the title is once more to revest in the grantor in possession and enjoyment; * * *."

It is clear that the Commissioner by thus relying upon Article 166–1, as amended in 1936, injected into the case prior to its consideration by the Board the theory that the taxpayer-settlor in view of the nature of the trust should be regarded as in substance the owner of the trust corpus. It would, we submit, be difficult to present this theory more plainly.

The taxpayer at no time objected to the Board's consideration of this theory of substantial ownership of the trust corpus. Instead, he stated the broad position of the Commissioner and answered it on the merits. The reply brief for the taxpayer before the Board first observes (Appendix B, *infra*, p. 57):

> It is to be noted that, in the Commissioner's deficiency letter (Petition, paragraph 2 and Exhibit A thereto), the position was taken that the trust involved "was a revocable trust and, therefore, the net income is taxable to the grantor." The respondent seems to have definitely abandoned the position that this is a revocable trust, * * *.

The taxpayer's brief then discusses the merits of the Commissioner's contentions, as follows (Appendix B, *infra*, p. 57):

> The next step [in the Commissioner's argument] * * * is that there was a regulation in effect in 1934 (part of Article 166–1, Regulations 86) providing that the grantor is regarded as in substance the owner of the corpus if it is apparent that he has failed to part permanently and definitively with the substantial incidents of ownership in the corpus, and that, the petitioner being in substance the owner of the corpus because it will ultimately come back to him, the income is taxable to him. The answer to this proposition is plain: The regulation as sought to be applied in this case goes beyond the pertinent statutory provision itself, and, seeking to make taxable what was expressly excluded from taxation by the statute itself, is null and void. * * *

At no time did the taxpayer argue before the Board that he was prejudiced or surprised by the Commissioner's reliance upon the amended regulations or that an opportunity should be given to him to adduce other facts. Compare *Helvering* v. *Edison Securities Corp.*, 78 F. (2d) 85 (C. C. A. 4th); *Underwood* v. *Commissioner*, 56 F. (2d) 67 (C. C. A. 4th); *Bankers Realty Syndicate*, 20 B. T. A. 612.[6]

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[6] Compare the cases permitting amendment of the petition or answer after submission of the case, but prior to decision: *Minnesota Tea Co.* v. *Commissioner*, 76 F. (2d) 797 (C. C. A. 8th), aff'd, 296 U. S. 378; 34 B. T. A. 145, rev'd, 89 F. (2d) 711, aff'd, 302 U. S. 609; *Excelsior Motor Mfg. & Supply Co.* v. *Commissioner* 43 F. (2d) 968 (C. C. A. 7th); *Enameled Metals Co.* v. *Commissioner*, 42 F. (2d) 213 (C. C. A. 3d).

2. The Circuit Court of Appeals (R. 29) remarked that "The issue presented to the Board was whether section 166 applied to a trust in which the estate reverted to the settlor after a period of years. The stipulated facts were framed with this issue in view." This statement, if construed to mean that such issue or theory of liability was the sole one before the Board, is not correct and must be the result of a misunderstanding. The Board nowhere states in terms that such a theory was the only one before it (R. 17). In truth it could not make such a finding. The briefs of the parties quoted immediately above show that a much broader question was presented to and argued before the Board prior to the Board's consideration of the case. There is nothing to suggest, and much to refute, the assumption that the taxpayer was in any way prejudiced or misled as to the scope of the issue before the Board.

The ninety-day letter of the Commissioners, it is true, explains the deficiency by stating only that under Section 166 the trust was a revocable trust (R. 7). But it is beyond doubt that the reasons given in the Commissioner's deficiency letter do not in any way operate as a limitation upon the scope of the issues or theories that may be raised before the Board. The appeal to the Board is from a final determination of a deficiency, not from the ninety-day letter, and the question there is not whether the Commissioner gave the right reason for his conclusion but whether he reached the right determination, whatever course of reasoning he may have followed.

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Helvering v. *Gowran*, 302 U. S. 238, 246; *Alexander Sprunt & Son* v. *Commissioner*, 64 F. (2d) 424, 427 (C. C. A. 4th).[7]

Furthermore, the Board's rules of practice indicate that the issues on appeal to the Board are determined by the pleadings of the parties.[8] Rules 6, 14, 15, 16, 17, 18, and 30, *infra*, Appendix E, pp. 69–70. The petition and answer in this case disclosed that the issue before the Board was the broad one as to the taxability of the trust income to the taxpayer-settlor (R. 3–8). The petition after setting forth the facts of the case alleges at item 4 (a) (R. 3) that—

> The determination of tax set forth in said notice of deficiency is based upon the following errors: (a) The Commissioner of Internal

[7] "It is immaterial whether the commissioner proceeded upon the wrong theory in determining the deficiency. In any event the burden was on petitioner to show that the assessment was wrong." *J. & O. Altschul Tobacco Co.* v. *Commissioner*, 42 F. (2d) 609, 610 (C. C. A. 5th). Accord: *Atlantic Bank & Trust Co.* v. *Commissioner*, 59 F. (2d) 363 (C. C. A. 4th); *James P. O'Laughlin*, 30 B. T. A. 1327; *Gossett* v. *Commissioner*, 22 B. T. A. 1279, aff'd on another issue, 59 F. (2d) 365, 60 F. (2d) 484 (C. C. A. 4th); *Edgar M. Carnrick*, 21 B. T. A. 12, 21.

[8] The statutory authority for the rules of the Board is found in Section 907 (a) of the Revenue Act of 1924, as amended, *infra*, Appendix D, p. 66. See *Goldsmith* v. *Board of Tax Appeals*, 270 U. S. 117.

> Revenue erred in including in the income of petitioner the net income arising under the trust established by the petitioner on December 29, 1930, as amended June 3, 1932, the beneficiary of which was his wife, Nannie C. Richter.

The answer of the Commissioner constitutes in effect a general denial (R. 8). Thus the question was squarely presented to the Board of Tax Appeals whether the trust income was taxable to the settlor. The hearing and subsequent briefs offered the first occasion for the parties to bring out the facts and present the legal theories with reference to them. But in the case at bar the hearing was entirely *pro forma:* the stipulation was agreed upon in advance and made a part of the record, without further testimony or argument before the Board Member (Appendix D, *infra*, p. 60). Hence it was not until the briefs were actually filed that the questions of law respecting the taxability of the trust income could be crystallized. Likewise from the standpoint of settled Board practice there is no doubt that the theory of substantial ownership could properly be advanced in the briefs. *Helvering* v. *Bowen*, 85 F. (2d) 926 (C. C. A. 4th). See *Schweitzer* v. *Commis-*

sioner, 75 F. (2d) 702 (C. C. A. 7th), reversed on other grounds, 296 U. S. 551.[9]

Moreover, it may be noted, the stipulation of facts was entered into some nine months after the pleadings were filed (R. 8–16). The taxpayer, if dissatisfied with the breadth of the question framed by the pleadings, could have moved under Rule 18.[10]

[9] See Charles E. Clark, Handbook of the Law of Code Pleading (p. 30):

> The aim of pleadings should be therefore to give reasonable notice of the pleader's case to the opponent *and to the court*. This does not go so far as the technical notice pleading, since it requires notice of the pleader's entire cause, not merely that he has a claim. The notice to the court is perhaps the more important, for in general the opponent knows enough about the case to relieve us of worry about him. In fact we have spent altogether too much thought over the danger of surprising the defendant. * * * The main purpose of the pleadings should therefore be to give the trial court a proper understanding of the case.

It has been observed (Paul & Mertens The Law of Federal Income Taxation, Vol. 5, p. 160, note 11):

> Although Dean Clark's comments were directed to the necessity that pleadings give notice to trial courts, they are even more applicable to the Board of Tax Appeals because the Board—composed as it is of members well steeped in the technique of tax matters—is less apt to be "surprised" by a shift of position which may follow amended pleadings.

[10] Rule 18 reads as follows (Appendix E, *infra*, p. 69):

"The Board, upon motion of either party in which good cause is shown, or upon its own motion, may order a further and better statement of the nature of the claim or defense, or of any matter stated in any pleading. Such a motion filed by a party shall point out the defects complained of and the details desired. * * *"

to make more definite the Commissioner's statement of the nature of his defense. Instead, he was apparently content to argue that under no theory could the trust income be taxed to him. It is not necessary, however, to indulge in speculation on this score. The conclusive evidence has already been noted, namely, the action of the taxpayer in answering on its merits, without any claim of prejudice, the broad argument of the Commissioner that under Article 166–1, as amended, the taxpayer-settlor remained in substance the owner of the corpus (pp. 19–20, *supra*). Since the theory of substantial ownership under Article 166–1 as amended was properly raised and argued before the Board there would appear to be no need to ascertain whether the Board specifically passed upon it. The Board, in any event, nowhere states in terms that the theory was not raised and argued before it (R. 17).

3. It may be noted, at this point, that the Commissioner in his brief before the Board (Appendix A, *infra*, pp. 54–55) mentioned only Section 166 and did not specify Section 22 (a) as the statutory basis upon which is rested Article 166–1 of Regulations 86 as amended in 1936. But this fact, we submit, has no bearing on the scope of the question raised and presented to the Board by his reliance upon Article 166–1 as thus amended.

The amended article discloses on its face that it is not based solely upon Section 166 nor restricted to the types of trusts therein defined with particularity; it rests upon Section 22 (a) also. *Helvering* v. *Clif-*

ford, 309 U. S. 331, 334n. It likewise expresses the same theory as to tax liability adopted by this Court in the *Clifford* case. Thus the taxpayer was put squarely on notice that the theory of substantial ownership embodied in Article 166–1 as amended and in Section 22 (a) was asserted to be applicable and determinative in this case. Compare *Helvering* v. *Wood*, 309 U. S. 344, 349n; *Commissioner* v. *Berolzheimer*, decided December 23, 1940, 1941 C. C. H. par. 9156 (C. C. A. 2d).

The Commissioner never expressed any intention to narrow the question—framed by his reliance upon Article 166–1 as amended in 1936—whether this theory was applicable and determinative here. He insisted, at all times, that the theory that the grantor remains in substance the owner of the corpus was fully applicable in view of the essential nature of the trust. He also insisted that the amended regulations embodying this theory of taxability were reasonable and within his statutory authority. In support of the statutory validity of the amended regulations, which in fact rest on Section 22 (a), the Commissioner cited only Section 166. But he certainly did not waive or abandon Section 22 (a). Nor did he waive his contention that the theory embodied in the regulations was applicable to the trust under consideration. His sole omission before the Board, if it can be so termed, was merely the failure to specify the precise statutory provision on which the amended regulations were rested. This, we submit, in no way detracted from the force of his contention that the amended regulations and the theory therein expressed

were applicable to this case. Their presumptive validity as well as their terms—disclosing that they are not confined to Section 166—militate against any such disregard of the applicability here of the regulations and the theory of substantial ownership therein expressed.

4. In his petition for review in the Circuit Court of Appeals the Commissioner again urged that the income of the trust was attributable to the taxpayer-settlor under Article 166–1 of Regulations 86 as amended by Treasury Decision 4629 (1936) (R. 20, 23). Subsequently, however, as a result of the supervening decisions in *Helvering* v. *Clifford*, 309 U. S. 331, and *Helvering* v. *Wood*, 309 U. S. 344, the Commissioner in his "Statement of Points" sought to tax the trust income to the taxpayer-settlor under Section 22 (a) (R. 23). About the same time, in his brief, the Commissioner waived reliance upon Section 166 (Appendix C, *infra*, p. 59).

The question before this Court is whether the Commissioner, who had fully argued before the Board the applicability of the amended regulations and the theory of substantial ownership therein expressed, could on appeal advance Section 22 (a) in support of their validity under the Act. The sole reason for refusing him this opportunity, it appears, is that in urging the theory embodied in Article 166–1, as amended, which in fact rests upon Section 22 (a), the Commissioner did not in his argument expressly refer to this precise statutory tag. The question may conveniently be discussed under two headings: (a) whether the Commissioner could support the

validity of Article 166–1 as amended under Section 22 (a); and (b) whether the Commissioner could support the validity of the theory of substantial ownership under Section 22 (a).

(a) Article 166–1 of Regulations 86 as amended by Treasury Decision 4629 (1936) was, unless invalid, fully applicable to the tax year in question. Regulations 86 govern income tax liability under the Revenue Act of 1934 covering the tax years 1934 and 1935. The year 1936 and subsequent years are governed by the Revehue Act of 1936 and later Acts. The 1936 amendment to Regulations 86 therefore would have been entirely without meaning unless it were to apply to the years 1934 and 1935, the only years covered by the 1934 Act. The scheme of the revenue acts, moreover, contemplates that changes in regulations are to relate to all tax years governed by the regulations unless the Secretary of the Treasury or the Commissioner affirmatively provides that the change shall have only prospective application. The relevant statutory provision (Appendix E, *infra*, p. 62) states that—

> The Secretary, or the Commissioner with the approval of the Secretary, may prescribe the extent, if any, to which any ruling, regulation, or Treasury Decision, relating to the internal revenue laws, shall be applied without retroactive effect. [Section 1108 (a) of the 1926 Act, as amended by Section 506 of the 1934 Act.]

The legislative history of this provision, which fully supports our contentions, is set forth at length in our brief for the respondent in *Guggenheim* v. *Rasquin*, No. 92, this Term, to which we respectfully refer the Court. Compare *Helvering* v. *Clifford*, 309 U. S. 331, 334n.

The 1936 amendment, moreover, cannot be thought invalid solely because of this retroactive application. It amended Article 166–1, it is true, so as to rest upon Section 22 (a) as well as Section 166. *Helvering* v. *Clifford*, 309 U. S. 331, 334n. But the criteria governing taxability remained essentially the same and no new rule of liability was created. Thus the amendment merely sharpened the legal theory already incorporated in the article and rested the article upon two sections of the 1934 Act instead of one. See *Morrissey* v. *Commissioner*, 296 U. S. 344. The case of *Helvering* v. *Reynolds Tobacco Co.*, 306 U. S. 110, is plainly distinguishable. The amended regulations there were were directly contrary to prior regulations that had been uniform for many years.

In view of *Helvering* v. *Clifford*, 309 U. S. 331, there would appear to be no other reason for not sustaining the amended regulations. The criteria stated to be controlling in the *Clifford* case (309 U. S. at 335–337) do not differ in any material respect from the governing criteria described in Article 166–1 as amended. It therefore follows that the amended as well as the original regulations are well within the

area of discretion conferred by Congress on the Commissioner.

A word may be added here with respect to *Helvering* v. *Wood*, 309 U. S. 344. There the Commissioner before the Circuit Court of Appeals failed to mention the amended regulations in his assignments of error (Record in this Court in No. 384, October Term, 1939, pp. 17–18) and in his brief expressly waived reliance upon any section other than Section 166 (309 U. S. at 348–349). By so doing, of course, he waived reliance upon the only provision of the Act—Section 22 (a)—that could support the theory that the grantor who, even without a power to revoke, retains sufficient incidents of ownership should be regarded as owner in substance or that could support the amended regulations insofar as they embody the same theory (309 U. S. 344, 346–348). This Court observed (309 U. S. at 348–349):

> The Board of Tax Appeals purported to place its decision solely on § 166 and § 167 of the Act. Petitioner in his assignments of error specifically mentioned only § 166 and § 167, not § 22 (a). In his brief before the Circuit Court of Appeals petitioner expressly waived reliance upon any section other than § 166. * * * In view of these facts, especially the express waiver below, we do not think that petitioner should be allowed to add here for the first time another string to his bow. * * *

The Commissioner in the *Wood* case thus narrowed the case in the Circuit Court of Appeals to the single

question [11] whether Section 166 was broad enough to support the theory of substantial ownership, apart from power to revoke, either as expressed in the *Clifford* case or as expressed in the amended regulations. The Circuit Court of Appeals answered that question, and no other, and this Court in the circumstances was not willing to overrule the court below when it had answered correctly the only question on which its opinion was sought.

The question as to scope of review in the *Wood* case, moreover, was not whether the Circuit Court of Appeals correctly decided the issues before it, for it had done so, but whether this Court would exercise its discretionary jurisdiction in favor of a litigant who had abandoned the only ground for a decision in his favor. The citation of *Burnet* v. *Commonwealth Improvement Co.*, 287 U. S. 415, 418, lends support to the view that the *Wood* case was intended to state the correct practice under such circumstances in this Court, not the practice in the circuit courts of appeals. The reliance placed in the *Wood* opinion upon the express waiver in the court below is also an indication that the Commissioner in the absence of such waiver would have been allowed to urge Section 22 (a) in that court as well as in this Court. Each of these factors, as well as the com-

[11] The Commissioner's brief before the Circuit Court of Appeals stated (p. 5):

"* * * the Commissioner bases this appeal solely on the question whether or not such income is taxable under Section 166 of the 1934 Act."

bination, serves to distinguish the *Wood* case from the case at bar.

In this case the Commissioner had not, as he had done in the *Wood* case, expressly waived Section 22 (a) upon which amended Article 166–1 rests. And this Court is not being asked to exercise its discretionary jurisdiction to consider and find applicable a theory of taxability that the tribunal below was misled into believing was abandoned except insofar as it was supported by Section 166. Here, in contrast, the applicability of the theory of substantial ownership as expressed in Article 166–1 as amended and in Section 22 (a) to the transaction of trust under scrutiny was in fact raised and urged at every step by the Commissioner, before the Board (pp. 16–27, *supra*).

The Government's position here is supported by several considerations:

The taxpayer, in the first place, cannot reasonably contend that the Commissioner's reliance upon Section 22 (a) in the Circuit Court of Appeals in any way surprised or prejudiced him. The applicability of Section 22 (a)—that is the theory implicit in Section 22 (a)—to the facts of this case had been fully raised and argued before the Board (pp. 16–27, *supra*). The taxpayer had ample opportunity there to meet that point, and, if possible, show on the stipulated facts or on others that might have been adduced that the trust transaction did not fall within the criteria which the Commissioner asserted were applicable.

The only point not presented in complete detail by the Commissioner before the Board was the precise section of the Act that as a matter of law supported the theory of taxability embodied in the regulations asserted to be applicable. It might well be contended that, since the regulations are presumptively valid, the burden was on the taxpayer to show that the theory expressed in Article 166–1 as amended could not possibly be supported under any section of the Act, including Section 22 (a) upon which it rests. Surely, we submit, the Commissioner does not have the burden of sustaining the validity of the regulations in the first instance. But, in any case, the point of law raised by the Commissioner's reliance upon Section 22 (a) could be met just as adequately in the Circuit Court of Appeals as before the Board.

The taxpayer, of course, may contend that in the Board the facts bearing upon the applicability of the theory there urged by the Commissioner were not adequately developed. The Government doubts that any facts can be brought forward that could possibly aid the taxpayer's cause (pp. 47–48, *infra*). The Commissioner, moreover, can scarcely be held responsible for the failure of the taxpayer to produce the facts to meet the theory of substantial ownership raised and argued before the Board. The Government is not attempting to gain an undue advantage. It seeks merely the right to support the validity as a matter of law of the amended regulations and the

theory they embody against what the *Clifford* case shows is an erroneous attack (pp. 29–30, *supra*).

The propriety of urging on appeal new reasons to support the validity of a theory of taxability argued in the Board is well established. This case is well within the rule applied in *Helvering* v. *Gregory*, 69 F. (2d) 809 (C. C. A. 2d), affirmed, 293 U. S. 465. There the Commissioner had contended before the Board that the transfers in question were inoperative and that the transaction as a whole constituted merely a dividend declaration. The Board found that the transfers were real and expunged the deficiency. The Second Circuit agreed with the Board that real transfers of title had actually taken place but concluded that the transaction as a whole lacked business purpose and, therefore, was outside the scope of the Act. Here, too, the Commissioner contended that the transfer in trust was inoperative for tax purposes since the grantor retained substantial incidents of ownership. The *Gregory* case would appear to be clear authority that on appeal the Commissioner could point to Section 22 (a) as the correct statutory basis for his contentions. Here, it may be observed, the Commissioner is not even shifting his theory in any way but is merely adding a reason for sustaining its validity. Accord: *Seufert Bros. Co.* v. *Lucas*, 44 F. (2d) 528, 530 (C. C. A. 9th).

An analogous case is *Helvering* v. *Leonard*, 310 U. S. 80, 83. The Government there sought in the

Circuit Court of Appeals to hold taxable the grantor of an alimony trust under Section 22 (a) of the applicable revenue act. It urged that Section 22 (a) was applicable for two reasons: one, that the continuing obligation of the grantor was unnecessary for taxability, and two, that in any event the applicable New York law relating to the modification of alimony decrees supplied the continuing obligation if one were necessary. The Circuit Court of Appeals ruled against the Government on both grounds. 105 F. (2d) 900. Upon certiorari, the Government renewed both grounds and added a third, not theretofore mentioned in the litigation, namely, that the grantor's guaranty of bonds, which constituted a substantial portion of the corpus, furnished the continuing obligation. This Court permitted the Government to make the new contention, and actually decided it in the Government's favor, recognizing at the same time that it had not been considered by the court below. 310 U. S. at 83. The case, at the very least, shows that this Court permitted an additional reason to be advanced in support of a theory of taxability, namely, existence of a continuing obligation. The rule thus applied would clearly permit Section 22 (a) to be advanced here in support of the theory of substantial ownership embodied in Article 166–1 as amended which was fully argued before the Board, especially since the amended article in fact rests upon Section 22 (a). *Helvering* v. *Clifford*, 309 U. S. 331, 334n.

The *Leonard* case may well stand for the even broader proposition that even a new theory may be advanced on appeal where the facts have been adequately developed. Accord: *Seufert Bros. Co.* v. *Lucas*, 44 F. (2d) 528, 530 (C. C. A. 9th); *United States* v. *Spaulding*, decided October 21, 1940 (C. C. A. 5th); see *White* v. *Higgins*, decided December 12, 1940 (C. C. A. 1st).

Likewise, the discussion in *Commissioner* v. *Berolzheimer*, December 23, 1940 (C. C. A. 2d), supports the contention that Section 22 (a) could be urged on appeal here. There, as in the case at bar, the Commissioner advanced before the Board the theory of substantial ownership without specific mention of Section 22 (a) but with reliance in part upon Section 166. In a well-reasoned opinion the court ruled:

> It is argued that the government cannot raise before this court the question of the applicability of Sec. 22 (a) because it did not raise that point before the Board of Tax Appeals. This contention is plainly unsound. While it is true that at the hearings before the Board the government relied partly on Sec. 166, which relates to taxation of income from revocable trusts, it also contended that the provisions of each trust instrument gave the grantor such control over the corpus of the trust that "in reality there was no trust." * * * The government is doing no more here than giving new reasons why the income of the trusts is taxable against the settlors under Section 22 (a). * * *

The Government also respectfully directs the Court's attention to the authorities and reasoning relied upon in Point II, *infra*, pp. 16–38. They show that the Circuit Court of Appeals in this case should have considered even a new theory of taxability under the circumstances. It follows that the actual case at bar—in which the Commissioner is merely advancing a new reason in support of a theory of tax liability fully argued before the Board—is well within the argument urged under Point II.

It is not entirely clear from the terms of the writ whether this Court will pass upon the question whether the Circuit Court of Appeals should have considered the applicability of Article 166–1 as amended in 1936 and its validity under Section 22 (a). But, if it is open, then we submit that the amended regulations should have been so considered.

(b) It is likewise clear that the Circuit Court of Appeals should have considered the theory presented by Section 22 (a) as construed in *Helvering* v. *Clifford*, 309 U. S. 331. The amended regulations upon which the Commissioner specifically relied both before the Board and the Circuit Court of Appeals in fact rest in part upon Section 22 (a) (p. 27, *supra*). They also express the same theory as to tax liability which is expressed by Section 22 (a) as construed in the *Clifford* case (p. 29, *supra*). In these circumstances it would be anomalous to hold

that the theory implicit in Section 22 (a) was not properly before the Circuit Court of Appeals.

It may be noted in this connection that the retroactive features of the 1936 amendment have no relevance whatever with respect to the breadth of the question properly raised before the Circuit Court of Appeals. To state an extreme case, by way of example only, the 1936 amendment might be held invalid because retroactive but still the theory as phrased in the amended regulations would be properly raised. The Commissioner, whether justified or not, did place his reliance upon the amended regulations as governing the tax year in question. Compare *Helvering* v. *Wood*, 309 U. S. 344, 349n. By so doing, he framed a question as broad as that framed by Section 22 (a) and gave notice, to all who read the terms of the amended regulation, that the ultimate statutory basis for taxability was other than Section 166. The case of *Helvering* v. *Wood*, 309 U. S. 344, as we have indicated (pp. 30–32, *supra*), in no way militates against the force of our contentions.

It is therefore submitted that the decision of the court below was erroneous and should be reversed with directions to consider and dispose of the case under Section 22 (a) of the Revenue Act of 1934 and Article 166–1 of Regulations 86 as amended.

II

SECTION 22 (A) SHOULD HAVE BEEN CONSIDERED EVEN THOUGH THE THEORY OF SUBSTANTIAL OWNERSHIP WAS NOT RAISED BEFORE THE BOARD

The argument under this point assumes, contrary to our understanding of the facts (pp. 16–27, *supra*), that the theory of substantial ownership of the trust corpus was not raised or argued before the Board. The assumption will be indulged that "The issue presented to the Board was whether section 166 applied to a trust in which the estate reverted to the settlor after a period of years" and that "The stipulated facts were framed with this issue in view" (R. 29). Even in that posture, we submit, the case should have been considered and disposition made under Section 22 (a). Our contention may be viewed as posing two distinct questions, first, whether the court below had power to dispose of the case under Section 22 (a), and if so, whether directions should be given to exercise that power under the circumstances here disclosed.

1. (a) At the outset the Court's attention is respectfully directed to the group of cases applying the oft-repeated rule that an appellee may support the judgment under review by reliance upon any ground consistent with the record. *Langnes* v. *Green*, 282 U. S. 531; *Helvering* v. *Gowran*, 302 U. S. 238, 245–246, and cases therein cited. It is settled that the rule is applicable to the review of decisions of the Board of Tax Appeals. *Helvering* v. *Gowran*, 302

U. S. 238, 246; *Helvering* v. *Rankin*, 295 U. S. 123, 132–133. As Mr. Justice Brandeis stated for the Court in the *Gowran* case (302 U. S. at 246):

> The taxpayer sought review of the Board's decision by the Court of Appeals. The ultimate question before that court was whether, upon the facts stipulated, the Board had erred in affirming the Commissioner's determination that the additional taxes were due. If the Commissioner was right in his determination, the Board properly affirmed it, even if the reasons which he had assigned were wrong. And, likewise, if the Commissioner's determination was right, the Board's affirmance of it should have been sustained by the Court of Appeals, even if the Board gave a wrong reason for its action.

It should be noted that, in the *Gowran* case, the Commissioner was permitted to rely upon an issue never before raised even though the taxpayer apparently had not established before the Board all the facts that could affect the result. The taxpayer was therefore granted leave to apply to the Circuit Court of Appeals for that purpose. 302 U. S. at 247.

If the Commissioner as of right may raise an entirely new issue upon appeal to sustain the Board, even though the case must be remanded, one may doubt the existence of any blanket rule denying the circuit courts of appeals power ever to consider a new theory advanced by the Commissioner when, perchance, the Board decision is against him.

(b) The decisions show that this Court has no want of power to reverse a judgment under review upon a theory not theretofore presented. A recent example in the tax field is found in *Helvering* v. *Leonard*, 310 U. S. 80, 83. Accord: *Seufert Bros. Co.* v. *Lucas*, 44 F. (2d) 528, 530 (C. C. A. 9th). Another situation in which this Court will consider or order considered a new issue or theory not theretofore argued is illustrated by *Erie R. R. Co.* v. *Tompkins*, 304 U. S. 64; and *Ruhlin* v. *New York Life Ins. Co.*, 304 U. S. 202.[12] During this Term the Court has asserted its power to consider errors of a fundamental nature whether raised or not. (*Sibbach* v. *Wilson & Company, Inc.*, No. 28, this Term, and cases cited. And the rule has been laid down that a supervening change in law or fact is substantial ground for reversing a judgment right when made. See cases cited, *infra*, pp. 50–52.

A somewhat analogous practice may be found in the settled rule that this Court, without finally disposing of a case, has power to remand the case for further proceedings where the trial was had upon the wrong theory or the record does not permit of final disposition with justice to all parties concerned. In cases arising from the inferior federal courts the power to vacate the judgment and remand for further proceedings has been exercised with liberality in a wide variety of situations. E. g., *United States* v. *Shelby*

[12] See also *New York Life Ins. Co.* v. *Jackson*, 304 U. S. 261; *Rosenthal* v. *New York Life Ins. Co.*, 304 U. S. 263.

Iron Co., 273 U. S. 571, 579; *United States* v. *Rio Grande Dam Co.*, 184 U. S. 416, 423; 215 U. S. 266, 275; *New York Central & H. R. Co.* v. *Beaham*, 242 U. S. 148, 152; *Jones* v. *Meahan*, 175 U. S. 1, 29; *Wiggins Ferry Co.* v. *Ohio & Miss. R. Co.*, 142 U. S 396, 413; *Liverpool Steam Co.* v. *Phenix Ins. Co.*, 129 U. S. 397, 447; *Combs* v. *Hodge*, 21 How. 397, 408; *Crocket* v. *Lee*, 7 Wheat. 522, 527; *Watts* v. *Waddle*, 6 Pet. 389, 402.

(c) This Court, moreover, has never laid down any blanket rule prohibiting a circuit court of appeals from considering any issue except one fully argued before the Board. The case of *General Utilities Co.* v. *Helvering*, 296 U. S. 200, stands for no such proposition. The opinion in that very case referred to the merits of the new issue not argued before the Board (295 U. S. 207). Accord: *Helvering* v. *Salvage*, 297 U. S. 106, 109. The reason for thus considering the new issue is stated in the opinion (296 U. S. at 207): "To remand the cause for further findings would be futile. The Board could not properly find anything which would assist the Commissioner's cause." The inference from the language is plain. The judgment should be reversed and the case remanded to the Board for consideration of the new issue unless the record shows that the Commissioner cannot prevail on the correct rule of law as applied either to the existing findings or to such as might be made. Section 1141 (c), Internal Revenue Code, Appendix E, *infra*, p. 65. *Legg's Estate* v. *Commissioner*, 114 F. (2d) 760, 767 (C. C. A. 4th), and

cases therein cited. Compare *White* v. *Higgins*, decided December 12, 1940, C. C. H. par. 9136 (C. C. A. 1st).

The power to reverse the Board upon a new issue, with or without such a remand, is fully supported by the statutory provision governing review of Board cases by the circuit courts of appeals. The statute reads (Section 1141 (c), Internal Revenue Code, *infra*, p. 65):

> Upon such review, such courts shall have power to affirm or, if the decision of the Board is not in accordance with law, to modify or to reverse the decision of the Board, *with or without remanding the case for a rehearing*, as justice may require. [Italics supplied.]

This affirmative command to dispose of the case "as justice may require" should not be ignored in determining the appropriate disposition upon appellate review of the Board's action. *Helvering* v. *Taylor*, 293 U. S. 507, 515–516; *Legg's Estate* v. *Commissioner*, 114 F. (2d) 760, 767 (C. C. A. 4th).

(d) The existence of the power to reverse a decision of the Board upon an issue or theory not there argued has been affirmed on many occasions. One of the most forceful statements in support of the validity of this practice is found in a recent opinion by Judge Parker (*Legg's Estate* v. *Commissioner*, 114 F. (2d) 760, 767 (C. C. A. 4th)). He there observed:

> We are given power by statute, 26 U. S. C. A. Int. Rev. Code § 1141 (c), "to affirm

> or, if the decision of the Board is not in accordance with law, to modify or to reverse the decision of the Board, with or without remanding the case for a rehearing, as justice may require." This is a broad power; and, if we are of opinion that the decision of the Board is not in accordance with law, we see no reason why we may not reverse its decision as justice may require, even on a point not raised before it. Just as we are emerging from the technicalities that formerly beset practice in courts of law and equity, it would be most unfortunate if we should develop a new system of technicalities to thwart and hamper the administration of justice in the ever increasing number of cases which come to us from administrative boards. * * *

His remarks find marked justification in the variety of occasions on which this asserted power has been exercised for the purpose of doing justice and equity in the inferior federal courts. E. g., *Seufert Bros.* v. *Lucas*, 44 F. (2d) 528 (C. C. A. 9th); *Chatham-Phenix Nat. Bank* v. *Helvering*, 87 F. (2d) 547, 550 (App. D. C.); *Edwards* v. *Holland Banking Co.*, 75 F. (2d) 713, 715 (C. C. A. 8th); *Hamilton Gas Co.* v. *Watters*, 75 F. (2d) 176, 182 (C. C. A. 4th); *Roosevelt* v. *Mo. State Life Ins. Co.*, 70 F. (2d) 939, 944 (C. C. A. 8th); *Eau Claire Book & Stationery Co.* v. *Commissioner*, 65 F. (2d) 125, 126 (C. C. A. 7th); *Underwood* v. *Commissioner*, 56 F. (2d) 67 (C. C. A. 4th); *Virginia-Lincoln Furniture Corp.* v. *Commissioner*, 56 F. (2d) 1028 (C. C. A. 4th).

It may be emphasized, once again, that the question here is not whether this Court in the exercise of its discretionary jurisdiction would, or should, consider an issue or a theory not fully argued before the lower courts. Cases in which this Court has chosen to ignore issues not raised in the petition for certiorari or argued here for the first time are completely beside the point. The question under consideration at this point is one of power, not discretion. The decisions holding that the circuit courts of appeals have that power are, we submit, fully supported by the analogous precedents in this Court and should be approved. It follows that the decision of the court below holding that, even if it wished, it lacked power to dispose of the case under Section 22 (a) (R. 29–30) was erroneous and should be reversed.

5. The question remains whether, assuming that it has the power, the Circuit Court of Appeals should be directed to make a disposition of this case under Section 22 (a). Whether or not a circuit court of appeals must always consider whatever theory is raised before it without regard to whether the theory was argued before the Board, nevertheless, in the case at bar the circumstances militate most strongly in favor of a disposition under Section 22 (a).

(a) The record shows beyond doubt that, whether or not it was affirmatively urged upon the Board (under Point I, *supra*, pp. 16–38, we contend it was), the theory of substantial ownership was never waived or abandoned by the Commissioner (R. 3–8, 20, 23). The Commissioner under established Board practice

would have been free under the pleadings to make the argument in the brief and have it considered by the Board (pp. 22–24, *supra*). It is equally clear that the Board itself could have raised the theory of substantial ownership and could have decided the case upon that theory.[13] The appeal to the Board is an appeal from a final determination of a deficiency. The duty of the Board essentially is to redetermine the correct tax liability of the taxpayer involved (pp. 21–22, *supra*).

The case at bar (viewed most favorably to the taxpayer) therefore discloses a situation in which a theory of liability—substantial ownership under Section 22 (a)—that might have been raised either by the Board or the parties, was overlooked and not directly called to the Board's attention. Since its disposition of the case, however, a supervening decision of this Court[14] has shown that this theory beyond doubt is applicable to the controversy and probably is determinative of the merits in favor of the Commissioner (pp. 47–48, *infra*). In future cases it is reasonable to assume the Board of its own motion will dispose of controversies like the present under Section 22 (a) (p. 20, *supra*). And the parties to such controversies, in any event, are not likely to overlook the theory spelled out in the

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[13] See *Helvering* v. *Gowran*, 302 U. S. 238, 246; *Minnesota Tea Co.* v. *Commissioner*, 76 F. (2d) 797 (C. C. A. 8th), aff'd, 296 U. S. 378; 34 B. T. A. 145, rev'd, 89 F. (2d) 711, aff'd, 302 U. S. 609; *Helvering* v. *Edison Securities Corp.*, 78 F. (2d) 85, 90–91 (C. C. A. 4th).

[14] *Helvering* v. *Clifford*, 309 U. S. 331.

Clifford case. The question here, then, in essence is this—whether some inflexible doctrine of appellate review militates against deciding the case at bar upon what appeal was only then clearly perceived to be the real merits of the controversy.

(b) In the case at bar, it is important to note, a disposition under Section 22 (a) may be made without the investigation of any transaction other than the transaction of trust under consideration by the Board. The stipulated facts in this case disclose all the terms of the instruments of trust (R. 11–16). These terms, we submit, are adequate to render the income chargeable to the taxpayer irrespective of what other evidence could be brought forward on his behalf. Such other evidence, whatever its character, could not possibly negative the fact that the corpus of the trust for the benefit of taxpayer's wife will be returned to him free of the trust within a period of five years. The grantor of a trust for so short a period in favor of a member of his family must be regarded as remaining in substance the owner of the corpus. Article 166–1 as amended by Treasury Decision 4629 (1936); *Helvering* v. *Clifford*, 309 U. S. 331. The fact, if it be a fact, that the wife had substantial income from other sources; that no restriction was placed on her use of the trust income; that such income was placed in her personal account and used for her private purposes; and that the trust was not designed or used to relieve the taxpayer from household expenses—this is all immaterial here. The contrary might well furnish additional reasons for

holding the taxpayer chargeable with the trust income. But absence of these other strings in no way detracts from the control exercised by the taxpayer through his power within five years to receive back the corpus, *Helvering* v. *Clifford*, 309 U. S. 331, at 333; Article 166–1 as amended by Treasury Decision 4629 (1936).

It follows that this case falls within the decisions holding that an appellate court should apply the correct rule of law wherever the facts have been adequately developed. E. g., *Helvering* v. *Leonard*, 310 U. S. 80, 83; *Seufert Bros. Co.* v. *Lucas*, 44 F. (2d) 528 (C. C. A. 9th); *White* v. *Higgins*, decided December 12, 1940, 1941, C. C. H., par. 9136 (C. C. A. 1st); *United States* v. *Spaulding*, decided October 21, 1940 (C. C. A. 5th).

The leading authority as to the correct practice to be followed by the circuit courts of appeals—the *General Utilities* case—does not militate against our position. By referring to the merits of the new issue, the opinion indicates that, even in the situation there disclosed, the Commissioner may have the proceeding remanded to the Board in the event his position is meritorious (p. 42, *supra*). Accord: *Helvering* v. *Salvage*, 297 U. S. 106, at 109. The *Clifford* case shows that our position here is meritorious.

The *General Utilities* case, in any event, is plainly distinguishable. The issue there sought to be raised for the first time upon appeal required an investigation of a transaction distinct from the transaction relevant to the issue argued before the Board and

urged in the petition for review. The argument to the Board was that taxable gain was realized by a corporation upon the distribution of appreciated assets to its stockholders (296 U. S. 200, 202–204). The new issue urged for the first time in the brief upon appeal was whether a sale of the appreciated assets by the stockholders, following the distribution, was carried through as agent for the corporation (296 U. S. at 204–205). Thus the sale by the stockholders which all parties before the Board viewed as a separate, unconnected transaction was sought to be brought into the controversy upon the appeal to the circuit court of appeals. In order to sustain the Commissioner upon the new issue the circuit court of appeals was compelled to make "an inference of fact directly in conflict with the stipulation of the parties and the findings" (296 U. S. at 206–207). Compare *Helvering* v. *Salvage*, 297 U. S. 106. No such conflict in facts or investigation of another transaction would result from a disposition of this case under Section 22 (a).

(c) Finally, we submit, the instances in which this Court has ordered that disposition of a case be made in the light of a supervening decision are clear warrant for directing the Circuit Court of Appeals to do the same here. The action of the parties and the Board indicate that, in a real sense, the precise theory of liability and its statutory basis as spelled out in the *Clifford* case was not well understood or well established—even though it was incorporated in the amended regulations—at the time this case was

argued before the Board (pp. 45–47, *supra*). The situation here may well be compared with the following:

(1) *Blair* v. *Commissioner*, 300 U. S. 5, arose upon this state of facts. A circuit court of appeals held that the taxpayer was chargeable with the income of a trust since under the law of Illinois the trust was a spendthrift trust and the assignments of income were invalid. *Commissioner* v. *Blair*, 60 F. (2d) 340. This Court denied certiorari. 288 U. S. 602. Subsequently, the State courts decided that the trust was not a spendthrift trust and upheld the assignments. *Blair* v. *Linn*, 274 Ill. App. 23. This Court recognized that ordinarily the prior decision as to taxability would be *res judicata* but that, since the local law was material to the controversy, the supervening State decision created a changed situation. It therefore considered the case on the merits. 300 U. S. at 8–9. The issue whether the assignments were valid, it may be noted, had been fully tried out in all the federal courts open to the taxpayer. Yet, several years later, the same issue was permitted to be retried in the federal courts. Suppose that, in the case at bar, the Government had failed to contest the Board decision and had merely assessed a deficiency for the following year. Under the *Blair* decision, we submit, there scarcely can be any doubt that the Commissioner could sustain such deficiency before the Board by reliance upon Section 22 (a) as construed in the supervening *Clifford* case. If *Blair* is authority for such an exception to the doctrine of *res judicata*, as it is, then surely it is

authority for our reliance upon *Clifford* when, as here, that supervening decision was issued during the process of litigation. This Court recently stated the controlling rule in *Vandenbark* v. *The Owens-Illinois Glass Co.*, No. 141, this Term:

> While not insensible to possible complications, we are of the view that, until such time as a case is no longer *sub judice*, the duty rests upon federal courts to apply state law under the Rules of Decision statute in accordance with the then controlling decision of the highest state court.

We submit that sound analysis, as well as the decisions relied upon in the quoted opinion, leads to the conclusion that inferior federal courts are under a duty to apply the law in accordance with the then controlling decisions of this Court. See *Trapp* v. *Metropolitan Life Ins. Co.*, 70 F. (2d) 976, (C. C. A. 8th), affirmed on rehearing, 72 F. (2d) 374, certiorari denied, 293 U. S. 596.

(2) Numerous cases are set out in the margin [15] in which disposition was made in the light of a supervening decision material to the real merits of the

[15] *Gulf Colorado & S. F. Ry. Co.* v. *Dennis*, 224 U. S. 503; *Dorchy* v. *Kansas*, 264 U. S. 286; *Patterson* v. *Alabama*, 294 U. S. 600; *Trapp* v. *Metropolitan Life Insurance Co.*, 70 F. (2d) 976 (C. C. A. 8th), affirmed on rehearing, 72 F. (2d) 374, certiorari denied, 293 U. S. 596; *Sioux County* v. *National Surety Co.*, 276 U. S. 238; *Oklahoma Packing Co.* v. *Oklahoma Gas Co.*, 309 U. S. 4, 8; *Moores* v. *National Bank*, 104 U. S. 625.

controversy. A supervening statute [16] or treaty [17] or change in material facts [18] likewise has been the occasion for causing the reversal of a judgment, even one right when made. It would seem that, under these precedents, a judgment based upon an erroneous rule of law—where, as here, the correct rule of law was neither well understood nor well established—could surely be corrected upon appeal when a supervening decision of this Court has made the error so plain that all can see. The statutory provision that the circuit courts of appeals shall have power "if the decision of the Board is not in accordance with law" to dispose of the case "as justice may require" is a broad grant of authority that should not be exercised with a grudging hand.

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[16] *Missouri ex rel. Wabash Ry. Co.* v. *Public Service Commission*, 273 U. S. 126; *Dinsmore* v. *Southern Express Co.*, 183 U. S. 115; *Carpenter* v. *Wabash Railway Co.*, 309 U. S. 23.

[17] *United States* v. *Schooner Peggy*, 1 Cranch 103.

[18] *Duke Power Co.* v. *Greenwood County*, 299 U. S. 259; *Watts, Watts & Co.* v. *Unione Austriaca*, 248 U. S. 9, 21.

CONCLUSION

It is submitted that, for the reasons stated, the decision of the court below should be reversed with directions to dispose of the case under Section 22 (a) of the Revenue Act of 1934.

Respectfully,

FRANCIS BIDDLE,
Solicitor General.

SAMEUL O. CLARK, JR.,
Assistant Attorney General.

SEWALL KEY,
JOSEPH M. JONES,
WILLIAM L. CARY,
Special Assistants to the Attorney General.

EDWIN E. HUDDLESON, JR.,
Attorney.

APPENDIX A

Excerpt from Government's Board brief in this case (p. 18):

III

The provisions of Article 166–1 of Regulations 86, as amended, require that the income of the present trust be taxed to petitioner.

The facts of the instant case bring them squarely within the scope of Article 166–1 of Regulations 86, as amended by Treasury Decision 4629, *supra*, and specifically that part of the regulations which provides as follows:

"But the provisions of section 166 are not to be regarded as excluding from taxation to the grantor the income of other trusts, not specified therein, in which the grantor is, for the purposes of the Act, similarly regarded as remaining in substance the owner of the corpus. The grantor is regarded as in substance the owner of the corpus if, in view of the essential nature and purpose of the trust, it is apparent that the grantor has failed to part permanently and definitively with the substantial incidents of ownership in the corpus."

It is apparent from the nature of the trust that petitioner has failed to part permanently and definitively with the substantial incidents of ownership in the corpus of the trust. Petitioner merely provided that the income of the trust for a limited number of years should be paid to his wife unless he died before the expiration of the limited number of years or unless she died before such expiration. He provided that during all of this limited time

the corpus of the trust should be kept intact for return to him upon the happening of any one of the events which should terminate the trust.

Respondent contends that the regulations are reasonable and fairly represent the intended application of the provisions of Section 166 of the Revenue Act of 1934 and that the application of the regulations to the facts of the instant case clearly requires that the Commissioner's determination of deficiency for the year 1934 should be sustained.

APPENDIX B

Excerpts from the taxpayer's reply brief before the Board in this case:

> The petitioner in his principal brief argued that the income arising under the trust during the year 1934 was not taxable to the grantor for the reasons (among others): First, that the existence of a reversionary interest after the termination of the trust for years does not constitute a power to revest within the meaning of Section 166 of the Revenue Act of 1934; second, that the event of the revesting of the corpus upon the death of the grantor or the death of the beneficiary during the life of the trust does not constitute a power to revest in the grantor; and, third, that since the power to revest in the grantor was in conjunction only with the beneficiary of the income of the trust, who had a substantial adverse interest, the income arising under the trust was not taxable to the grantor. The respondent in its brief appears to have admitted all of these propositions and to have cast the decision of this case upon the determination of the issue of the taxability of income arising under a trust to the grantor, regardless of any other circumstances, if the trust is a trust for a definite term of years with the corpus thereof reverting to the grantor at the termination thereof. From the brief for respondent it is clear that (except for the ultimate issue of taxability to the grantor of the trust income) every issue presented in the petitioner's brief is admitted, including the fact that the bene-

ficiary of the income here, the grantor's wife, had a substantial adverse interest.

* * * * *

It is to be noted that, in the Commissioner's deficiency letter (Petition, paragraph 2 and Exhibit A thereto), the position was taken that the trust involved "was a revocable trust and, therefore, the net income is taxable to the grantor.". The respondent seems to have definitely abandoned the position that this is a revocable trust, and now argues that in any trust for years where upon the termination thereof the corpus returns to the grantor the income arising therefrom during the intervening period is taxable to him. * * *

* * * * *

The next step, which is necessarily based upon the false premise just discussed, is that there was a regulation in effect in 1934 (part of Article 166–1, Regulations 86) providing that the grantor is regarded as in substance the owner of the corpus if it is apparent that he has failed to part permanently and definitively with the substantial incidents of ownership in the corpus, and that, the petitioner being in substance the owner of the corpus because it will ultimately come back to him, the income is taxable to him. The answer to this proposition is plain: The regulation as sought to be applied in this case goes beyond the pertinent statutory provision itself, and, seeking to make taxable what was expressly excluded from taxation by the statute itself, is null and void. We sincerely doubt if the regulation just referred to was adopted to be applied to a situation such as is presented herein. However, as we point out later herein, no life can be breathed into

a plainly invalid regulation by the subsequent re-enactment of the same statute.

* * * * *

As sought to be applied by the respondent in this case, Regulations 86 ignore completely the language of the Congress, whereby it provided for the taxability of the income arising under a trust where the grantor "had the power", and fail utterly, if the present interpretation thereof sought to be applied be correct, to distinguish between the "termination" of the trust by its own terms and the "revocation" of the trust by some unfettered act of the grantor before its automatic termination under express provisions of he trust instrument. * * *

* * * * *

APPENDIX C

Excerpt from Government's Circuit Court of Appeals brief in this case (p. 7):

> In view of the decision in the *Wood* case, we are not here contending that Section 166 is applicable to the instant case. But we do believe and submit that Section 22 may properly be considered on this appeal and that under the *Clifford* case the Commissioner is entitled to a reversal here. See also *Helvering* v. *Hormel* (C. C. A. 8th), decided April 25, 1940, not yet officially reported but found in Vol. 4, Prentice-Hall, 1940, par. 62, 617.

APPENDIX D

Reporter's Minutes before Board of Tax Appeals:

HEARING AT WASHINGTON, D. C., ON THE 6TH DAY OF DECEMBER, 1938, AT 9:30 O'CLOCK A. M.

The above-entitled proceeding came on for hearing on this, the 6th day of December, 1938, before the HONORABLE EUGENE BLACK, Member of the United States Board of Tax Appeals, at Washington, D. C., pursuant to notice of hearing heretofore given; whereupon, the following proceedings were had, to wit:

APPEARANCE:

EDW. WOOLF, Esq., (HONORABLE J. P. WENCHEL, Chief Counsel, Bureau of Internal Revenue), appearing on behalf of the COMMISSIONER OF INTERNAL REVENUE, Respondent.

PROCEEDINGS

The CLERK. Docket No. 92208, O. G. Richter.

Mr. WOOLF. May it please Your Honor, Mr. Brewster appears for the respondent.

Mr. BREWSTER. If Your Honor please, we have agreed upon the facts in this case, and we have a stipulation covering the material facts.

The MEMBER. Then, suppose I hear you on the second call here in this room. You might want to make a statement about the issues.

Mr. BREWSTER. If Your Honor please, that is entirely satisfactory.

(Whereupon, the case was continued until the second call of the calendar.)

[The record contains no further reference to any "statement about the issues" at the hearing.]

APPENDIX E

Revenue Act of 1934, c. 277, 48 Stat. 680:

SEC. 22. GROSS INCOME.

(a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * * [U. S. C. Supp. V, Title 26, Sec. 22.]

SEC. 166. REVOCABLE TRUSTS.

Where at any time the power to revest in the grantor title to any part of the corpus of the trust is vested—

(1) in the grantor, either alone or in conjunction with any person not having a substantial adverse interest in the disposition of such part of the corpus or the income therefrom, or

(2) in any person not having a substantial adverse interest in the disposition of such part of the corpus or the income therefrom,

then the income of such part of the trust shall be included in computing the net income of the grantor. [U. S. C. Supp. V, Title 26, Sec. 166.]

SEC. 506. RETROACTIVITY OF REGULATIONS, RULINGS, ETC.

Section 1108 (a) of the Revenue Act of 1926, as amended, is amended to read as follows:

"(a) The Secretary, or the Commissioner with the approval of the Secretary, may prescribe the extent, if any, to which any ruling, regulation, or Treasury Decision, relating to the internal revenue laws, shall be applied without retroactive effect." [U. S. C., Title 26, Sec. 1691.]

Internal Revenue Code:

SEC. 1141. COURTS OF REVIEW.

(a). *Jurisdiction.*—The Circuit Courts of Appeals and the United States Court of Appeals for the District of Columbia shall have exclusive jurisdiction to review the decisions of the Board, except as provided in section 239 of the Judicial Code, as amended, 43 Stat. 938 (U. S. C., Title 28, § 346); and the judgment of any such court shall be final, except that it shall be subject to review by the Supreme Court of the United States upon certiorari, in the manner provided in section 240 of the Judicial Code, as amended, 43 Stat. 938 (U. S. C., Title 28, § 347).

* * * * *

(c) *Powers.*—

(1) *To affirm, modify, or reverse.*—Upon such review, such courts shall have power to affirm or, if the decision of the Board is not in accordance with law, to modify or to reverse the decision of the Board, with or without remanding the case for a rehearing, as justice may require.

* * * * *

Section 907 of the Revenue Act of 1924 as amended by Section 601 of the Revenue Act of 1928, provides in part as follows (c. 352, 45 Stat. 872):

The proceedings of the Board and its divisions shall be conducted in accordance with such rules of practice and procedure (other than rules of evidence) as the Board may prescribe and in accordance with the rules of evidence applicable in courts of equity of the District of Columbia.

Treasury Regulations 86, promulgated under the Revenue Act of 1934:

ART. 22 (a)–1. *What included in gross income.*—Gross income includes in general compensation for personal and professional services, business income, profits from sales of and dealings in property, interest, rent, dividends, and gains, profits, and income derived from any source whatever, unless exempt from tax by law. (See sections 22 (b) and 116.) In general, income is the gain derived from capital, from labor, or from both combined, provided it be understood to include profit gained through a sale or conversion of capital assets. * * *

Art. 166–1 (as amended by T. D. 4629, XV–I Cum. Bull. 140, 141 (1936)). *Trusts, with respect to the corpus of which, the grantor is regarded as remaining in substance the owner.*—(*a*) If the grantor of a trust is regarded, within the meaning of the Act, as remaining in substance the owner of the corpus thereof, the income therefrom is not taxable in accordance with the provisions of sections 161, 162, and 163 but remains attributable and taxable to the grantor. This article deals with the taxation of such income. As used in this article, the term "corpus" means any part or the whole of the property, real or personal, constituting the subject matter of the trust.

(*b*) Section 166 defines with particularity instances in which the grantor is regarded as in substance the owner of the corpus by reason of the fact that he has retained power to revest the corpus in himself. * * *

* * * * *

But the provisions of section 166 are not to be regarded as excluding from taxation to the grantor the income of other trusts, not specified therein, in which the grantor is, for the purposes of the Act, similarly regarded as remaining in substance the owner of the corpus. The grantor is regarded as in substance the owner of the corpus, if, in view of the essential nature and purpose of the trust, it is apparent that the grantor has failed to part permanently and definitively with the substantial incidents of ownership in the corpus.

In determining whether the grantor is in substance the owner of the corpus, the Act has its own standard, which is a substantial one, dependent neither on the niceties of the particular conveyancing device used, nor on the technical description which the law of property gives to the estate or interest transferred to the trustees or beneficiaries of the trust. In that determination, among the material factors are: the fact that the corpus is to be returned to the grantor after a specific term; the fact that the corpus is or may be administered in the interest of the grantor; the fact that the anticipated income is being appropriated in advance for the customary expenditures of the grantor or those which he would ordinarily and naturally make; and any other circumstances bearing on the impermanence and indefiniteness with which the grantor has parted with the substantial incidents of ownership in the corpus.

Thus the grantor is regarded as being in substance the owner of the corpus if, in any case, the trust amounts to no more than an arrangement whereby the grantor, in the ordering of his affairs, finds it expedient to entrust for a period the title to, and custody or management of, certain of his property to a trustee, the income from such property to be used by the trustee during such period to make those expenditures which the grantor would customarily or ordinarily or naturally make and to which the grantor chooses to commit himself in advance, while the corpus is to be held intact, for return in due course to the grantor. In such a case, it is immaterial that, at the time of the creation of the trust, an irrevocable disposition or consummated gift was made of those property rights which consist of the right to the expected future income of the corpus for the specified period. On the other hand, if the grantor, incident to a definitive and permanent disposition of certain of his property, creates the trust in order to conserve the property, not for himself but for the donees, who will ultimately enjoy it, the provisions of sections 161, 162, and 163 are applicable.

(*c*) For example, a grantor is regarded as remaining in substance the owner of the corpus of the trust, if he has placed it in trust for his son, John.

(A) for the term of three years, at the end of which time the trust might be extended for a like period at the option of the grantor and successively thereafter, but in the absence of such an extension the title is once more to revest in the grantor in possession and enjoyment; * * *

Rules of Practice before the Board of Tax Appeals:

Rule 6.—Initiation of a Proceeding—Petition.

A proceeding shall be initiated by filing with the Board a petition, as provided in Rules 4, 5, and 8, and substantially in accordance with Form 2, shown in Appendix I. The petition shall be complete in itself so as fully to state the issues. It shall contain:

* * * * *

PETITION

(b) Proper allegations showing jurisdiction in the Board.

(c) A statement of the amount of the deficiency [or liability, as the case may be], determined by the Commissioner, the nature of the tax, the period for which determined, and the amount thereof (as nearly as may be computed) in controversy.

(d) Clear and concise assignments of each and every error which the petitioner alleges to have been committed by the Commissioner in the determination of the deficiency. Issues in respect of which the burden of proof is by statute placed upon the Commissioner will not be deemed to be raised by the petitioner in the absence of assignments of error in respect thereof. Each assignment of error shall be numbered.

(e) Clear and concise numbered statements of the facts upon which the petitioner relies as sustaining the assignments of error, except those assignments of error in respect of which the burden of proof is by statute placed upon the Commissioner.

(f) A prayer, setting forth relief sought by the petitioner.

(g) The signature of the petitioner or that of his counsel. (See Rule 4.)

* * * * *

(i) A copy of the notice of deficiency [or liability, as the case may be], shall be appended to the petition. If a statement has accompanied the notice of deficiency, so much thereof as is material to the issues set out in the assignments of error likewise shall be appended. If the notice of deficiency refers to prior notices from the Bureau, which are necessary to elucidate the determination, such parts thereof as are material to the issues set out in the assignments of error shall likewise be appended. (See Appendix I, Form No. 2.)

Rule 14.—Answer

After service upon him of a copy of the petition, the Commissioner shall have 60 days within which to file an answer or 45 days within which to move in respect of the petition. The answer shall be so drawn as fully and completely to advise the petititioner and the Board of the nature of the defense. It shall contain a specific admission or denial of each material allegation of fact contained in the petition and a statement of any facts upon which the Commissioner relies for defense or for affirmative relief or to sustain any issue raised in the petition in respect of which issue the burden of proof is, by statute, placed upon the Commissioner. Each paragraph contained in the answer shall be numbered to correspond with the paragraphs of the petition. An original and four copies of the answer shall be filed, of which the original shall be signed by the Commissioner or his counsel and the copies conformed by him.

The clerk will serve one copy of the answer upon the petitioner or his counsel of record by registered mail.

Rule 15.—Reply

If the answer of the Commissioner sets forth facts upon which he relies for affirmative relief, or contains a statement of the facts upon which he relies to sustain an issue in respect of which the burden of proof is placed upon him by statute, the petitioner shall, within 45 days after a copy of such answer is mailed to him or his counsel of record by registered mail, file a reply which shall contain a specific admission or denial of each material allegation of fact contained in the answer and shall set forth any facts upon which he relies for defense. Each paragraph contained in the reply shall be numbered to correspond with the paragraphs of the answer. An original and four copies of the reply shall be filed, of which the original shall be signed by the petitioner or his counsel and the copies conformed by him.

The Board upon motion of the respondent in which good cause is shown, or upon its own motion, may require the verification of any reply.

The clerk will serve one copy of the reply upon the Commissioner.

Rule 16.—Joinder of Issue

A proceeding shall be deemed at issue upon the filing of the answer unless a reply is required under Rule 15, in which event the proceeding shall be deemed at issue upon the filing of the reply.

Rule 17.—Amended and Supplemental Pleadings

The petitioner may, as of course, amend his petition at any time before answer is filed. After answer is filed, a petition may be

amended only by consent of the Commissioner or on leave of the Board.

All motions to amend, made prior to the hearing, must be accompanied by the proposed amendments or amended pleading.

Upon motion made, the Board may, in its discretion, at any time before the conclusion of the hearing, permit a party to a proceeding to amend the pleadings to conform to the proof.

When motions to amend are granted at the hearing, the amendment or amended pleading shall be filed at the hearing or with the Board within such time as the member presiding may fix.

See Rules 4 and 19.

Rule 18.—Pleadings—General

The Board, upon motion of either party in which good cause is shown, or upon its own motion, may order a further and better statement of the nature of the claim or defense, or of any matter stated in any pleading. Such a motion filed by a party shall point out the defects complained of and the details desired. * * *

* * * * * *

Rule 30.—Submission Without Hearing or Appearance

(*a*) *Submission of cases without hearing where facts are uncontested.*—Any case not requiring a hearing for the submission of evidence (as, for example, where sufficient facts have been admitted, stipulated, or included in the record in some other way) may be submitted at any time by notice of the parties filed with the Board. The parties need not wait for the proceeding to be cal-

endared and need not appear in person. The Chairman will then assign the proceeding to a Division for report, which division, upon request of the parties, will fix a time for filing briefs or for oral argument.

(*b*) A contested motion, not predicated upon an issue of fact, may be submitted in the same way.

See, however, Rule 31.

Rule 31.—Evidence and the Submission of Evidence

* * * * *

(*b*) *Stipulations.*—The parties by stipulation in writing filed with the Board or presented at the hearing, may agree upon any facts involved in a proceeding. A complete duplicate of the stipulation, including all exhibits, shall be filed at the same time. Stipulations filed need not be formally offered to be considered in evidence.

* * * * *

(*f*) *Failure of proof.*—Failure to adduce evidence in support of the material facts alleged in the petition and denied by the Commissioner in his answer will be ground for dismissal. Where there is a joinder of issue on questions of fact, the provisions of Rule 30 do not relieve the party upon whom rests the burden of proof from properly producing evidence to support the issues.

Rule 32.—Burden of Proof

The burden of proof shall be upon the petitioner, except as otherwise provided by statute and except that in respect of any new matter pleaded in the answer, it shall be upon the respondent.

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